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UNCLAS SECTION 01 OF 07 ASTANA 002131

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SUBJECT: KAZAKHSTAN: 2009 NATIONAL TRADE ESTIMATE

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¶1. The following information responds to reftel request.

TRADE SUMMARY

The U.S. goods trade deficit with Kazakhstan was $618 million in 2008, an increase of $119 million from $499 million in 2007. U.S. goods exports in 2008 were $986 million, up 30.9 percent from the previous year. Corresponding U.S. imports from Kazakhstan were $1.6 billion, up 28.1 percent. Kazakhstan is currently the 76th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Kazakhstan was $4.9 billion in 2007(latest data available), up from $4.6 billion in ¶2006.

Kazakhstan has been negotiating membership in the WTO since January 29, 1996. As part of the process, Kazakhstan is still negotiating bilateral market access agreements with a number of WTO Members, including the United States, the EU, and Australia. In 2007, Kazakhstan signed market access agreements with Malaysia, Brazil, and Israel. Currently, 21 out of 40 Members of the WTO Working Party for Kazakhstan have signed bilateral market access agreements, the most recent of which were Canada and Australia. While progress was made in 2008, in implementing WTO-consistent legislation, more work remains in a number of areas, including reform of customs practices, sanitary and phytosanitary (SPS) regulation, technical barriers to trade (TBT), government procurement, and taxation.

The United States-Kazakhstan Bilateral Trade Agreement, which came into force in 1993, grants conditional normal trade relations treatment. A bilateral investment treaty came into force in January ¶1994.

IMPORT POLICIES

Kazakhstan is a member of the Eurasian Economic Community (EAEC), along with Russia, Kyrgyzstan, Belarus, Tajikistan, and Uzbekistan. Armenia, Moldova, and Ukraine currently have observer status. Five of the EAEC members (all but Uzbekistan) have formed a free trade area. In 2006, Kazakhstan, Russia, and Belarus announced the formation of a trilateral customs union. Significant progress was made in 2008 on formulating the underlying legal basis for the customs union. The progress included the Russian Duma's ratification of a free trade agreement, and agreements on the establishment of both regulatory and dispute resolution agencies in October 2008. Russia, Belarus, and Kazakhstan intensified consultations and negotiations in early 2009, and officially signed legal agreements for its creation on November 27 in Minsk. According to the agreements, a common external trade tariff will be enacted as of January 1, 2010. Kazakhstan's entrance into the Customs Union will increase its import tariffs, which already increased from 6.6 percent in 2008 to almost 13 percent in 2009 according to the Custom Committee of the Republic of Kazakhstan.

According to current Customs Union agreements, Kazakhstan will retain some flexibility in determining the common external import tariff regime. For example, according to officials from the Ministry of Industry and Trade, Kazakhstan will have no tariff on over 900 specific commodity items, including modern aircraft, certain types of engines, and raw materials needed in the food processing industry, such as tropical fruits. Over 400 specific commodity items will be subject to a transitional period varying from one-and-half to five years. These items include pharmaceuticals, medical equipment, processed aluminum products, raw materials for the petrochemical industry, paper products, rail wagons, combines, and tractors. In some specific cases, Customs Union member states also can apply protective import tariffs on

selected goods without the consent of the other members, but only for six months per year and for a maximum of five years. The member states have agreed to grandfather all previously existing protective and anti-dumping measures at the time of accession into the Customs Union. The Customs Union implementation timeline anticipates implementation of the new common Customs Code and abolishment of the Russian-Belarus customs border on July 1, 2010. The Kazakhstani-Russian customs border is scheduled for abolishment on July 1, 2011.

The Law on Investments, enacted in January 2003, provides customs duty exemptions for imported equipment and spare parts, but only if Kazakhstani-produced stocks are unavailable or not up to international standards. Despite the creation of the Customs Union, Kazakhstan is expected to continue to offer preferential treatment to investors outside of the extractive sector in an effort to promote economic diversification.

U.S. exporters to Kazakhstan have consistently identified the requirement to obtain a "transaction passport" (providing information on, inter alia, the importer, contract details, local bank of importer/exporter, and a foreign partner) to clear goods through customs as a significant barrier to trade. The transaction passports are designed to stem capital outflows and money laundering by requiring importers to show documents that verify the pricing of import/export transactions. In July 2006, the National Bank of Kazakhstan (NBK) enacted new regulations that simplified -- but retained -- the transaction passport requirement. Principal changes included elimination of the trade distorting maximum financing term of 180 days for imported goods and transfer of the authority to issue transaction passports from customs to the NBK and commercial banks. According to Kazakhstani regulations, the transaction passports contain concise information on trade partners and include a unique transaction code; specific payment information such as currency, means, and deadlines for payment; and complete contact information for contracting parties. Kazakhstan amended the Law on Currency Control in August 2009, thereby changing the ceiling on transactions from $10,000 to $50,000. Despite some internal Kazakhstani opposition to the transaction-passport system, the National Bank of Kazakhstan insists on its necessity to control capital movement and prevent capital flight.

In 2009, Kazakhstan established and later lifted, thanks largely to effective communication between the U.S. Department of Agriculture's (USDA) Animal and Plant Health Inspection Service (APHIS) and the Kazakhstani Ministry of Agriculture, several trade bans. For example, the appearance of H1N1 led to a ban on the import of all pork and pork products from Texas, California, and Kansas on June 5, 2009, which was lifted on October 19, 2009. Similarly, to address the perceived threat of Hemorrhagic disease, Kazakhstan banned all rabbits and rabbit products on December 10, 2008, which it lifted on October 19, 2009. During the same period, as a result of the perceived threat of Bovine Sponge Encephalitis (BSE), a ban on beef and beef products was established in December 2008 and removed in October 2009.

Although Kazakhstani officials are diligently addressing the problematic structure of Kazakhstan's customs control agencies, customs administration and procedural implementation remain a principal barrier to trade. Kazakhstan's planned entrance into the Customs Union has not negatively impacted its own attempts to streamline the customs process. Since August 2008, the Kazakhstani Customs Control Committee has been participating in a Parliamentary working group, convened at the direct request of the Prime Minister, to develop a new overhauled Customs Code, bring Kazakhstan's legislation into compliance with WTO standards, and remove several identified barriers to trade. Amendments currently being considered by President Nazarbayev are designed specifically to meet standards required for WTO accession and include declaration rights for

foreign citizens (bypassing the current legal requirement for the participation of domestic brokers), ex officio rights for customs agents, and standardized guidelines for the valuation of goods. Kazakhstani customs authorities expect approval of these amendments by the end of December with their entry into force the beginning of ¶2010.

STANDARDS, TESTING, LABELING, AND CERTIFICATION

In 2007, Kazakhstan adopted a number of laws in furtherance of its efforts to develop a national system of standardization and certification, such as laws on Safety of Chemical Products, Safety of Food Products, Safety of Toys, and Safety of Equipment and Machinery, as well as a series of amendments to the Law on Technical Regulation.

In 2008, this package of laws was augmented by the Law on Accreditation, which regulates the accreditation of entities that conduct conformity assessment.

The Kazakhstani Law on Technical Regulation distinguishes the state's responsibilities from those of the private sector. The government is responsible for establishment of product safety standards, but delegates quality control responsibilities to authorized private institutions. A wide range of goods are subject to mandatory certification requirements, which apply to both domestically-produced and imported goods. A related regulation lists the specific categories of products subject to certification, including machines, cars, agricultural and telecommunication equipment, construction materials, fuel, clothes, toys, food, and drugs.

The Law on Technical Regulation requires that contracts for the delivery of imported goods include a special clause which confirms the goods comply with Kazakhstani standards. Delivery contracts must also be accompanied by documents that describe the products and list the country of origin, the producer, the expiration date, any storage requirements, and instructions for the use of the product in both the Kazakh and Russian languages. In addition, the law states that foreign certificates, testing protocols, and compliance indicators must be in accordance with international treaties. Kazakhstani authorities normally recognize foreign certificates, but the verification process can take 10-25 days depending on the industry.

The National Accreditation Center of Kazakhstan intends to become a

full member of the International Laboratory Accreditation Cooperation in 2010 and the International Accreditation Forum in ¶2012. It is currently developing legislation to accomplish this goal. This step would automatically make the Kazakhstani National Accreditation Center a signatory to a number of international treaties on metrology and standards.

President Nazarbayev's National Program for Accelerated Industrial and Innovative Development announced in May 2009 and the Russia-Belarus-Kazakhstan (RBK) Customs Union might affect technical regulatory policies in Kazakhstan, by incorporating new industrial standards based on international best practices and a harmonized system of technical regulation designed largely to comply with WTO standards.

GOVERNMENT PROCUREMENT

Some potential U.S. suppliers have raised concerns about the transparency and efficiency of Kazakhstan's government tender process. Corruption and lack of transparency remain major challenges for both local and foreign companies.

In July 2007, Kazakhstan enacted the Law on Government Procurement,

which was designed to increase the transparency of the procurement process and provide relevant state agencies with greater operational flexibility. Concurrent amendments to the Administrative Code stipulated administrative penalties for violations of the Law on Government Procurement. In November 2008, Parliament approved amendments to this Law on Government Procurement, which became effective in December 2008. The amendments are primarily designed to further reduce corruption and introduce an e-procurement system. As mandated by President Nazarbayev, the changes to the Law on Government Procurement should also enhance the participation of domestic suppliers in government procurement, and whenever possible, give preference to them.

During the first half of 2009, Kazakhstan adopted regulations and amendments to several laws designed to increase the proportion of local content in government procurement procedures. The exact proportion of the required purchase of local goods and services is calculated according to a specific formula, which was approved by Kazakhstan's Foreign Investor Council. It will be applied to domestic and foreign operators in Kazakhstan, including government agencies, state-owned enterprises, national holding companies such as Samruk-Kazyna, and subsoil users. According to new tender requirements, proposals that include significant proportions of locally-produced goods and services will receive preferential treatment. Conversely, tender commissions without them will be charged administrative fees and may face administrative prosecution. The Kazakhstani government is elaborating its official concept for the development of Kazakhstani content. A mandate of substantial increases by 2014 in the local-content share of Kazakhstani-produced goods (up to 50 percent) and Kazakhstani-produced services (up to 90 percent) is expected.

Kazakhstan's largest national companies, governed under the umbrella of the Samruk-Kazyna national holding company, including Kazakhstan TemirZholy (national railway), KazMunayGas (national oil and gas company), KEGOC (electricity transmission company), and other companies with their subsidiaries are subject to the local-content requirements, but are thus far exempted from the Law on Government Procurement.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

The Kazakhstan government's effort to diversify the economy away from the energy sector and spur the growth of a domestic high technology industry, combined with the WTO accession process, has led to a strong emphasis on IPR protection. Kazakhstan is currently considering a number of changes to its IPR legislation that will strengthen IPR protection and provide tools for improved IPR enforcement.

In 2009, Kazakhstan adopted several amendments to IPR legislation,

including the legal recognition of vendors who possess associated rights for the distribution of print and digital media. This amendment allows licensed vendors to seek damages from unauthorized dealers selling pirated merchandise that is otherwise properly licensed internationally for resale. Kazakhstan also amended its patent law to re-define a patent holder, including detailed descriptions of the relationship between an employer and an employee with respect to an employee's invention.

Although domestically-produced pirated films and music are available in Almaty and Astana. Thanks largely to decreasing costs of making copies, the vast majority of pirated goods in these regions appear to be imported, predominantly from Russia and China. Armed with statutes enacted in November 2005 that authorize stiffer penalties for infringers, the authorities have conducted numerous raids against distributors of pirated products. The government's efforts have greatly helped to expand the Kazakhstani market for licensed, non-infringing products. Still, much remains to be done,

particularly in ensuring that Customs controls are applied more effectively against imported infringing goods. Legislation to strengthen intellectual property protection and enforcement is under Presidential review, including a proposal to grant customs officials' badly-needed ex officio power to seize infringing goods at the border. Amendments to trademark legislation are being developed.

Further progress is also needed in the realm of civil enforcement, which is serving as an increasingly prevalent method of IPR enforcement. Although civil courts have been used effectively to stem IPR infringement, judges often lack expertise in the area of IPR, which is a significant obstacle to further improvement in Kazakhstan's IPR climate.

SERVICES BARRIERS

Foreign ownership of individual mass media companies, including news agencies, is limited to 20 percent in accordance with Kazakhstan's law "On National Security," Article 22, Paragraph 5, Number 4. Foreign banks and insurance companies are limited to operating in Kazakhstan through joint ventures with Kazakhstani companies. For certain professional services, including auditing, architectural, urban planning, engineering, integrated engineering, and veterinary services, commercial presence is allowed only in the form of a juridical person. For telecommunication services, foreign ownership may not exceed 49 percent, also in accordance with Kazakhstan's above-referenced law "On National Security. "

INVESTMENT BARRIERS

Kazakhstan's 2003 Law on Investments provides the legal basis for foreign investment in Kazakhstan. In general, U.S. investors have concerns about the law's narrow definition of investment disputes, its lack of clear provisions for access to international arbitration, and certain aspects of investment contract stability guarantees.

The vast majority of foreign investment in Kazakhstan is directed to the oil and gas sector. The Government remains eager to do business with international companies, but increasingly has emphasized the importance of "local content" in purchases of goods and services for petroleum operations. For example, a new draft Law on Subsoil and Subsoil Use, expected to be adopted in early 2010, contains explicit requirements regarding the local purchase of goods and services and the hiring of Kazakhstani nationals for all investments in offshore oil and gas exploration and production. This law could cause difficulties for international investors, because the methodology to calculate local content is not well defined, and Kazakhstani goods and services do not always fully comply with international standards. If enforced to the letter, the law could adversely affect the cost and schedule of contracts. The draft subsoil law also requires that KazMunayGas, the national oil company, have a minimum 51 percent share in all new exploration and production contracts, and it establishes a procedure through which the national oil company may obtain field rights outside of a tender process.

Taken together, these clauses appear to establish KazMunayGas as a necessary partner for international oil companies investing in Kazakhstan.

The proposed legislation would also require separate contracts for exploration and production operations, put shorter time limits on exploration contracts, enhance the government's authority to terminate contracts not in compliance with the law, and require tax stability clauses in individual contracts to be approved by parliament. In addition, under the terms of the legislation, no future contracts would be structured as production sharing agreements (PSAs), which allow companies to recoup capital expenditures before making royalty payments to the government.

Although exploration and production contracts would be separated, a company awarded exploration rights would nevertheless be given priority rights to negotiate a production contract with the government following an oil or gas discovery. However, if the terms of the production contract were not agreed to within a set time period, production rights would be opened to other bidders through a public tender.

The draft law also includes a preemption clause that guarantees the State the right of first refusal when a party seeks to sell any part of its stake in a mineral resource extraction project. The State claims this preeminent right even in cases where the controlling agreement assigns preemptive rights elsewhere (e.g., to other investors in a consortium). The proposed draft also fully incorporates an October 2007 amendment to the current subsoil law which allows the government to force amendments to existing subsoil contracts of "strategic significance" -- or even terminate such contracts -- where the economic interests of Kazakhstan are so threatened as to create a "national security risk." On August 1, 2009, the government passed Decree No.1213 on "Approving the List of Subsoil Fields having Strategic Significance." The list includes over 100 oil and gas fields, including Tengiz, Kashagan, and Karachaganak. This Decree fuels concerns over the stability of contracts. It authorizes the government to amend or change contracts if it determines that the actions of a subsoil user could lead to a substantial change in Kazakhstan's economic interests or threaten Kazakhstan's national security. The Decree provides no further guidance on how the government will define a change in economic interests or a threat to national security.

Kazakhstan's law allows citizens of Kazakhstan and foreigners to own land under commercial and noncommercial buildings, including dwellings and associated land. Such land may also be leased for up to 49 years. The land code, enacted in June 2003, for the first time allows private ownership by Kazakhstan's citizens of agricultural land, in addition to industrial, commercial, and residential land. An amendment enacted in July 2007 extends the right to own agricultural land to Kazakhstani owned businesses as well. Foreigners may still only lease agricultural land for up to 10 years.

Foreign investors continue to have difficulty obtaining work permits for employees who are not Kazakhstani nationals. Many companies report that permits for key managers and technicians are routinely rejected or granted for unreasonably short periods or are conditioned upon demands for additional local hires. Companies also report that hiring regulations are confusing and interpreted inconsistently by local officials and the Ministry of Labor and Social Protection.

In December 2007, Kazakhstan adopted new regulations on foreign labor. While the Ministry of Labor and Social Protection claims the new regulations simplify the issuance of work permits to foreigners, they impose additional requirements to support the domestic labor market that many investors find onerous.

In light of these difficulties for investors, the government has been increasing slightly the number of work permits available. In 2006, the number of permits was limited to 0.55 percent of the economically active population (estimated at about 8 million

people). The percentage figure was increased to 0.8 percent in 2007 (approximately 640,000 permits). For 2008, it was increased to 1.6 percent; and for managers and professionals it increased from 0.3 to 0.6 percent. For skilled workers, the quota rose from 0.37 percent to 0.93 percent.

OTHER BARRIERS

There are other structural barriers to investment in Kazakhstan, including a weak system of business law, a lack of an effective judicial system for breach of contract resolution, and an unwieldy government bureaucracy. Many companies serving the Kazakhstani market report significant logistical difficulties.

In addition, there is a burdensome tax monitoring system for all companies operating in Kazakhstan. Many companies report the need to maintain excessively large staffs in Kazakhstan to deal with the cumbersome tax system and frequent inspections. The actions of tax and various regulatory authorities, as well as actions to enforce environmental regulations, can be unpredictable. The government has, on occasion, initiated criminal cases against local employees of foreign firms. Kazakhstani authorities often require, as part of a foreign firm's contract with the government, that the firm contribute to social programs for local communities.

Widespread corruption at all levels of government is also seen as a barrier to trade and investment in Kazakhstan. It reportedly affects nearly all aspects of doing business in Kazakhstan, including customs clearance, registration, employment of locals and foreigners, payment of taxes, and the judicial system.

SPRATLEN